InvAsset's Voice



THE RISE, FALL AND FIGHTBACK

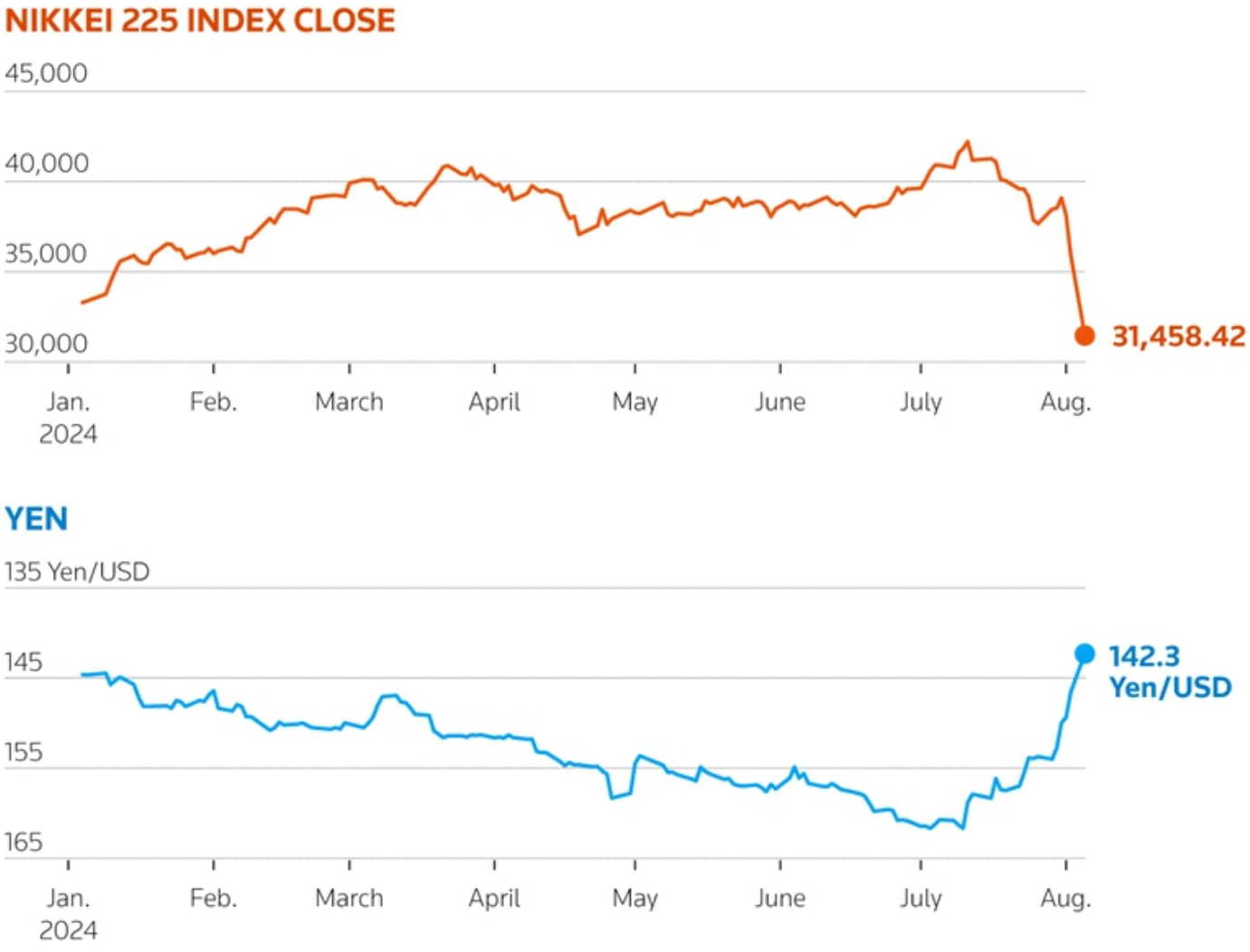
THE YEN'S ODYSSEY THROUGH TIME

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Nikkei vs yen

Japanese stocks collapsed on Aug. 5 in their biggest single day rout since the 1987 Black Monday sell-offs, driven by last week's plunge in global stock markets, economic concerns and worries investments funded by a cheap yen were being unwound.



Note: Data as of Aug. 5, 2024 0902GMT

Sources: LSEG Workspace

Pasit Kongkunakornkul • Aug. 5, 2024 | REUTERS

THE RISE, FALL AND FIGHTBACK

THE YEN'S ODYSSEY THROUGH TIME



**1986-1990: THE YEN'S GOLDEN PEAK

The Japanese yen stood tall during the late 1980s, bolstered by Japan's booming export-led economy. It reached unprecedented strength against the dollar, embodying the confidence of a nation reshaping global trade. However, this era of euphoria came crashing down as Japan's infamous asset price bubble burst in 1990, ushering in the **"Lost Decades"**—a prolonged period of economic stagnation and deflation.

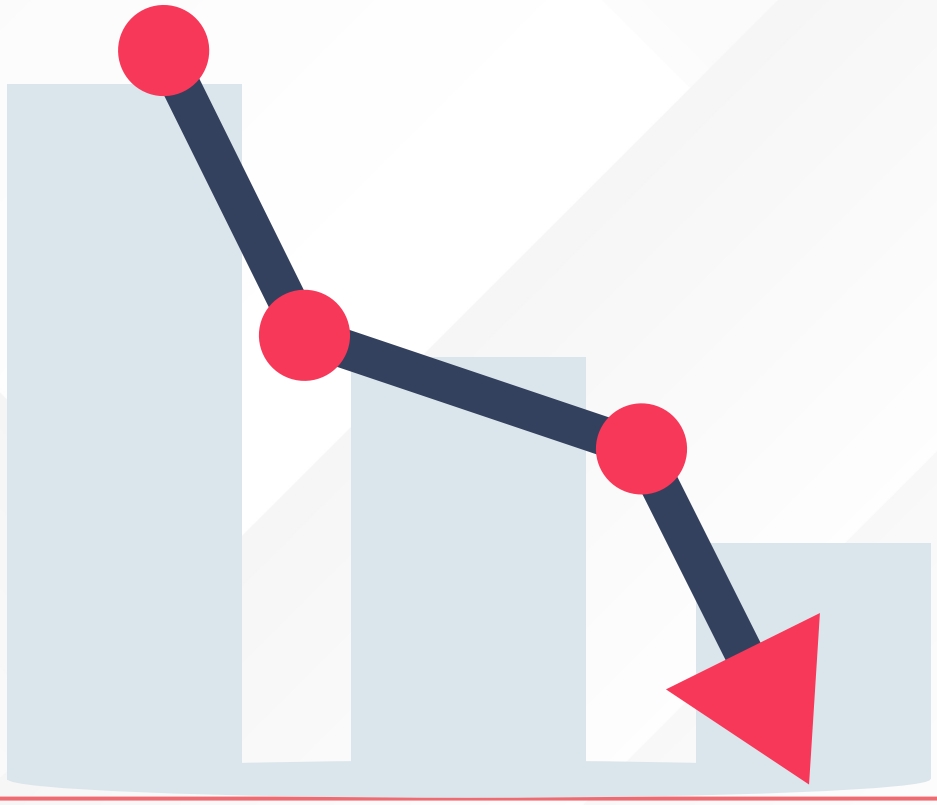


1991-1998: EARLY CRISES AND A FRAGILE CURRENCY

• **1991-1992:** The Bank of Japan (BOJ) began a pattern of intervention as the yen showed signs of instability, selling dollars to prop up its value.

• **1997-1998:** The Asian Financial Crisis sent shockwaves through Japan, destabilizing the yen. The BOJ's aggressive interventions stemmed some damage, but the crisis revealed the fragility of Japan's financial system.

These years were marked by a delicate balancing act, as Japan grappled with its slowing domestic economy while attempting to maintain stability in a volatile global market.



2011: A PRELUDE TO CHANGE

In late 2011, Japan faced a new economic reality. The BOJ intervened in currency markets, selling yen to prepare for a “massive monetary expansion” aimed at reviving its economy. This signaled a shift in priorities: rather than protecting the yen's strength, Japan began actively weakening it to support its export-driven recovery.



2021-2024: THE YEN'S RAPID DESCENT



· 2021: The yen entered a freefall as interest rate differentials between Japan and the U.S. widened. The Federal Reserve's aggressive rate hikes contrasted sharply with Japan's rock-bottom borrowing costs.

· 2022: Tokyo launched multiple interventions to defend the yen, spending $60 billion in September and October alone. Despite these efforts, the yen continued its slide, losing more than 20% of its value against the dollar.

· 2024 April-May: The yen plummeted to a 34-year low, trading at 160.86 against the U.S. dollar. The Ministry of Finance intervened again, but these efforts offered only fleeting relief.

July-August 2024: The yen surged 13% within weeks as BOJ signaled rate hikes, but this rebound triggered an unwinding of yen carry trades, wiping out profits for investors and sparking global market turmoil.

THE UNWINDING OF THE CARRY TRADE A GLOBAL RIPPLE EFFECT



For decades, the yen was the darling of the **carry trade**—a strategy where investors borrowed yen at low interest rates to invest in higher-yielding currencies. This strategy thrived on Japan's near-zero rates but began unraveling as the BOJ cautiously raised its benchmark to **0.25% in 2024.**

The unwinding triggered a sell-off in global markets, culminating in August 2024's **"Black Monday"** on the Nikkei 225 index, its worst single-day collapse since 1987. As investors offloaded yen-funded positions, global stocks and bonds spiraled into chaos.

THE YIN AND YANG OF A WEAK YEN

- **Drawbacks:**

o Import prices for essentials like fuel and food skyrocketed, inflating household costs and hurting retailers.

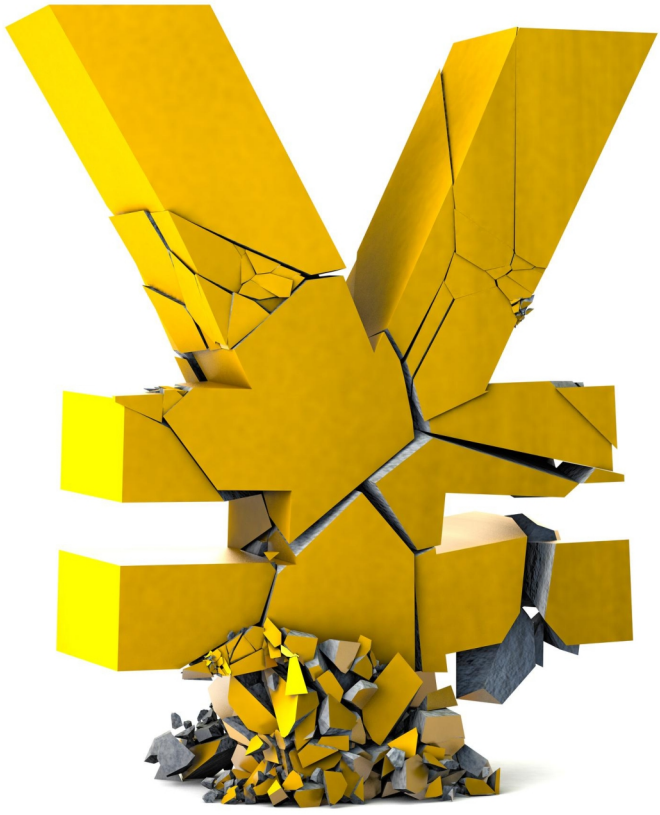
o Core inflation, driven by these costs, surpassed the **BOJ's 2% target for 27 consecutive months,** eroding domestic purchasing power.

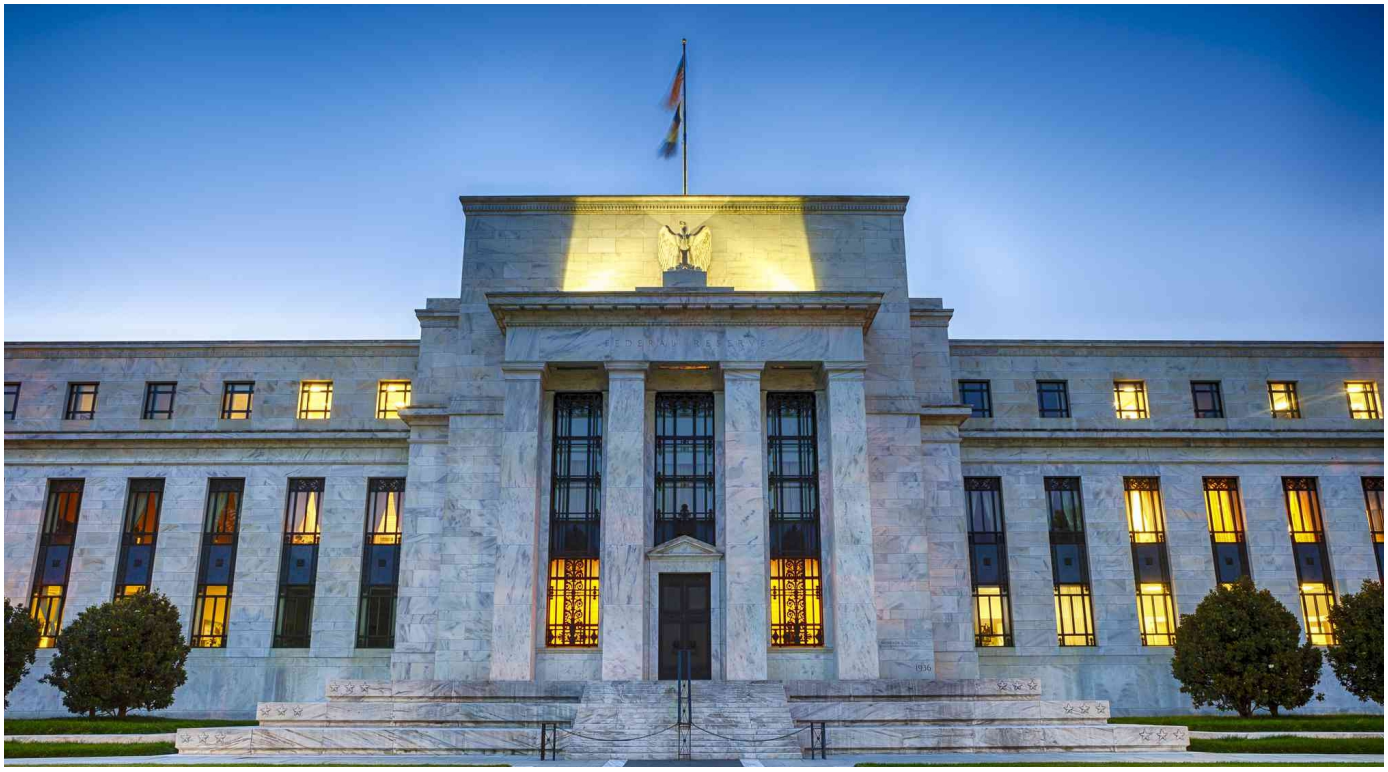
- **Benefits:**

o Exporters flourished as Japanese goods became cheaper on the global market, boosting profits.

o Tourism surged, with 3.1 million foreign visitors in March 2024 alone, revitalizing local businesses.

The weak yen, while painful for households, became a boon for Japan's global competitiveness, highlighting its dual-edged nature.



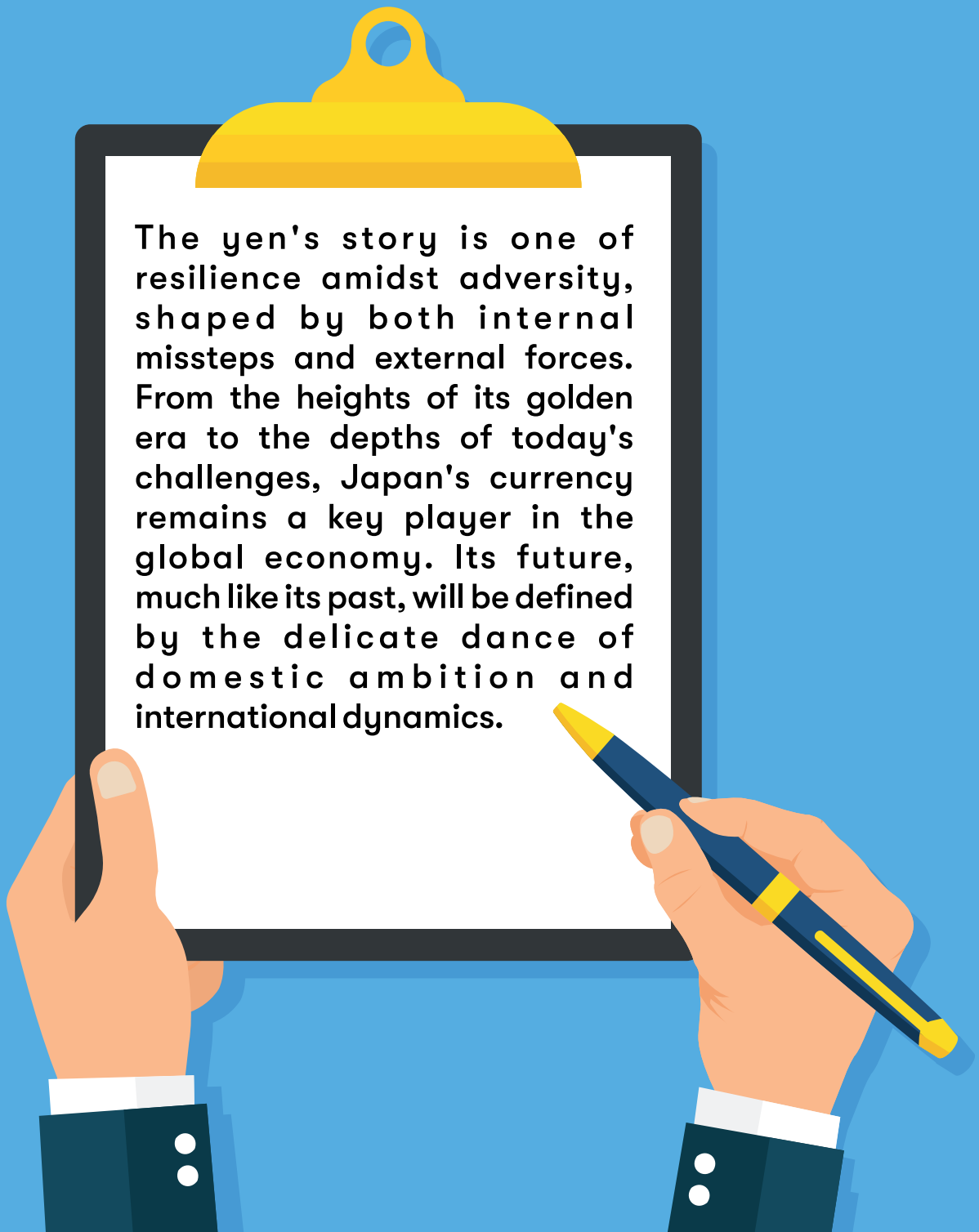


2024 AND BEYOND WHAT LIES AHEAD FOR THE YEN?

Japan's policymakers face a Herculean task. The BOJ's cautious rate hikes reflect fears of stalling consumption and worsening public debt, limiting their ability to act decisively. Currency interventions, though symbolic, have proven to be temporary fixes.

The yen's recovery depends largely on **external factors,** particularly the Federal Reserve's next moves. A potential slowdown in U.S. inflation could narrow the interest rate gap, offering the yen a lifeline. Until then, Japan remains at the mercy of global financial tides.

CONCLUSION
THE YEN'S JOURNEY THROUGH THE WINDS OF CHANGE



THE YEN'S ODYSSEY JAPAN'S CURRENCY AT A CROSSROADS

The Japanese yen, once a bastion of global financial stability, finds itself at a historic precipice. In 2024, the yen plummeted to its weakest value against the U.S. dollar since 1986, trading at 160.86. This stark decline underscores the fragility of Japan's economy, which has wrestled with stagnation and external pressures for decades. The confluence of factors fueling this slide paints a tale of diverging monetary policies, structural economic inertia, and the global ramifications of financial interconnectedness.

Why is the Yen Crumbling?

The yen's depreciation is largely a byproduct of a widening interest rate chasm between Japan and the United States. While the Federal Reserve has pursued aggressive interest rate hikes since 2022 to combat inflation, the Bank of Japan (BOJ) clings to its ultra-loose monetary stance, only recently nudging its rate from negative territory to 0.25%. This divergence fosters a "carry trade" phenomenon, where investors borrow yen at low rates to invest in higher-yield assets abroad, perpetuating downward pressure on the currency.

Moreover, Japan's prolonged struggle with stagnant wages and tepid inflation starkly contrasts with the U.S.'s robust economic growth and inflationary pressures. The yen, once a safe haven, has lost over one-third of its value since 2021, with no immediate reprieve in sight.

The Fallout of a Weak Yen

The implications of the yen's weakness are a double-edged sword. On one hand, exporters thrive, with Japanese goods becoming more competitive abroad, and tourism surges as visitors flock to the island nation, buoyed by favorable exchange rates. On the other hand, the cost of imports—especially fuel and food—has skyrocketed, eroding household purchasing power and inflating living costs.

Core inflation, driven by soaring import prices, has consistently outpaced the BOJ's 2% target for 27 months. For a nation heavily reliant on imported energy and raw materials, this marks a significant strain on retailers and consumers alike.

The Specter of Carry Trades

The yen's plight is further complicated by the unraveling of carry trades. This high-risk investment strategy—borrowing yen to invest in higher-yielding currencies like the U.S. dollar—has exacerbated market volatility. As Japan tentatively raises interest rates and the Federal Reserve hints at potential rate cuts, the profitability of these trades has evaporated, triggering a cascade of unwinding positions that roil global stock and bond markets.

In August 2024, Japan's Nikkei 225 index suffered its largest single-day drop since Black Monday in 1987, underscoring the fragile interplay between currency valuations and global market stability. The yen's 13% appreciation within a month—fueled by BOJ interventions—wiped out carry trade profits and rattled investor confidence.

The Path Forward



Japan faces a conundrum: how to stabilize the yen without jeopardizing its delicate economic recovery. While the BOJ has hinted at gradual rate hikes, its cautious approach reflects concerns over dampening domestic consumption and exacerbating public debt costs. Currency interventions, such as the $60 billion spent in 2022, have proven short-lived, failing to stem the yen's decline.

Ultimately, the yen's fate hinges on external factors—chiefly, the Federal Reserve's policy trajectory. If U.S. inflation subsides and rate cuts materialize, the interest rate gap could narrow, offering the yen a chance at redemption. Until then, Japan's currency remains a microcosm of the broader economic and geopolitical forces shaping the global financial landscape.

The yen's story is one of resilience and reinvention, caught between the weight of its past and the uncertainty of its future. Whether it reclaims its status as a symbol of strength or succumbs to the tides of change will be a defining chapter in Japan's economic odyssey.

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